

Testimony of

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**On Behalf Of the
National Association of Home Builders**

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Legislative Proposals on GSE Reform

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Introduction

Chairman Frank, Ranking Member Bachus and members of the Committee, my name is Jerry Howard and I am the Executive Vice President and Chief Executive Officer of the National Association of Home Builders (NAHB). The 235,000 members of NAHB appreciate the opportunity to present their views to the House Financial Services Committee on legislation to overhaul the regulatory oversight of the housing Government Sponsored Enterprises (GSEs) – Fannie Mae, Freddie Mac and the Federal Home Loan Banks (FHLBanks). The GSEs are critical components of the nation's housing finance system and are largely responsible for the efficiency and resiliency of that system, as reflected in the tremendous advances recorded in the availability and affordability of mortgage products for home buyers and providers of rental housing. The success and value of our housing finance system has been clearly evident in recent years from both a human perspective, as demonstrated by the record homeownership rate, and from an economic perspective, with the housing sector serving as an important engine of growth.

One of the reasons the GSE regulatory reform initiative is so challenging is because of the uniqueness of the U.S. housing finance system. This extremely efficient and liquid system is a blend of public and private components. The linchpin is a sophisticated secondary market that facilitates the flow of credit to housing from investors in the domestic and international capital markets. The system has evolved to provide a reliable supply of housing credit at relatively low and affordable mortgage interest rates from coast-to-coast, and during rising and falling economic cycles.

The U.S. housing finance system's public-private partnership framework is particularly prominent in the secondary mortgage market arena. At the core of the secondary market are the GSEs. Fannie Mae, Freddie Mae and the Federal Home Loan Banks are private entities, each with a public mission to provide liquidity to the housing finance system and lower housing borrowing costs. Studies show that the GSEs lower mortgage rates by as least 25 basis points, and NAHB estimates that this results in increased homeownership opportunities for approximately 1.2 million households.

To be sure, accounting scandals and corporate governance shortcomings present a disturbing picture to those who placed their trust in these entities to serve an important public purpose. NAHB agrees that the current GSE regulatory system would benefit from renovation and enhanced supervisory powers. To that end, NAHB appreciates your commitment to enacting legislation to improve the regulatory framework for the housing GSEs. NAHB supports the establishment of a regulator that can ensure that Fannie Mae, Freddie Mac and the Federal Home Loan Banks operate in a safe and sound manner and effectively pursue their housing mission. NAHB believes that the housing GSEs are essential components of the nation's housing finance system and our foremost interest is that change in the regulatory regime should not, in any way, diminish the benefits that these entities provide to home buyers and renters.

NAHB believes that the GSE bill passed in October 2005 by the House was a good start toward achieving this objective. We also commend the efforts undertaken in the closing days of the 109th Congress to reach compromise on issues that have been obstacles to further legislative

progress. That work seems to have provided traction for this year's deliberations. With the recent introduction of H.R. 1427, the "Federal Housing Finance Reform Act of 2007," NAHB is pleased to see a continuation of the ongoing bipartisan movement towards comprehensive GSE regulatory reform legislation.

Although there is a myriad array of factors and ingredients to consider in the reform debate, NAHB believes the optimal approach to GSE reform incorporates four guiding principles: First, the advantages inuring to the GSEs through the public/private partnership of the housing finance system should be retained. Second, reform measures should reinforce the obligation of the GSEs to channel those advantages to the nation's home buyers and renters. Third, the most efficient and demonstrable method of accomplishing this objective is through enhanced safety and soundness regulation and stronger GSE affordable housing requirements. Fourth, there must be a balance between safety and soundness oversight and mission regulation so as not to impede the GSEs' housing mission.

NAHB's views on the current GSE regulatory reform discussions can be effectively distilled down to six key components: (1) regulatory structure; (2) capital requirements; (3) portfolio limits; (4) program oversight; (5) conforming loan limits; and, (6) affordable housing requirements. The remainder of NAHB's statement addresses these components.

Regulatory Structure

An overriding issue in the GSE regulatory reform discussion is achieving the appropriate balance between safety and soundness and mission oversight in the structure and governance regime of the regulator. It is a priority for NAHB that Congress establishes a strong system for regulating the safety and soundness of the GSEs without displacing the focus on the housing mission of the GSEs.

Currently, the Department of Housing and Urban Development (HUD) oversees the mission of Fannie Mae and Freddie Mac, including approving new programs and establishing and enforcing affordable housing goals (annual mortgage purchase targets that Fannie Mae and Freddie Mac must reach). The Office of Federal Housing Enterprise Oversight (OFHEO), an independent agency within HUD, oversees the financial safety and soundness of Fannie Mae and Freddie Mac. For the FHLBanks, another independent agency, the Federal Housing Finance Board (FHFB) regulates both mission and financial safety and soundness.

Several questions have been raised as to how to better configure this oversight system. One area of inquiry with bearing on the mission/safety and soundness balance is the location and independence of the GSE regulator. NAHB believes the regulator should be an independent entity outside the control of any cabinet department or regulatory agency. The agency must have independence or autonomy in pursuing its regulatory duties. Thus, NAHB supports the provisions in H.R. 1427 that would establish a stand-alone regulator outside any other cabinet or government unit. Further, NAHB supports granting the regulator the authority over Fannie Mae, Freddie Mac and the FHLBanks.

Perhaps the greatest concern for NAHB in this area is the governance of a new GSE regulatory agency. H.R. 1427 would place control of the new regulator in the hands of a single director and would create an advisory board which would not have executive powers. The Board would be comprised of the Treasury and HUD Secretaries and the Director of the Federal Housing Finance Agency (FHFA), who would serve as Chairperson. Of significant concern, H.R. 1427 eliminates the provisions in the 2005 House bill that would have included two independent members on the advisory board. The independent members in the 2005 bill were required to have expertise in housing finance and capital markets activities and issues. NAHB opposes the limited board approach taken in H.R. 1427 because it removes the additional housing mission emphasis and capital markets perspective that the independent board members would convey. In addition, a regulator headed by a single individual and advised by a small board could be subject to political influence and might not exercise independent judgment. Also, such a structure would open the door for the regulator to take actions of tremendous importance without adequate accountability for such actions.

Ideally, NAHB believes the new regulator should be governed by a board modeled on the Federal Deposit Insurance Corporation (FDIC), where the board seats are divided between government representatives and private individuals with appropriate regulatory expertise. In the case of the GSE regulator, the board would be made up of the Secretaries of HUD and Treasury and three private individuals, one of whom would serve as the board chair. The goal is to infuse additional expertise in and concern for housing and housing finance through the appointment of individuals with such credentials. NAHB also would support the advisory board structure in the 2005 bill as an acceptable compromise solution.

As an additional counterbalance between mission and safety and soundness regulatory objectives, NAHB supports the creation of deputy director positions to oversee the various regulatory elements. In this regard, NAHB supports the three separate regulatory divisions provided for in H.R. 1427, including: oversight of safety and soundness for Fannie Mae and Freddie Mac, FHLBank regulatory oversight, and housing mission for all of the GSEs. NAHB encourages the Committee to ensure that the FHLBank mission and safety and soundness oversight reflects the unique mission, operating structure and charters of the FHLB System.

Capital Requirements

Capital requirements for financial institutions establish the level of reserves that these organizations must maintain to protect against their exposure to various types of risks, including credit risk of loans and guarantees, interest rate risk of the balance sheet, and management and other operational risk. Capital requirements also limit the degree to which financial institutions can leverage their sources of funds in pursuing business opportunities. Generally, financial institutions are held to two separate capital standards: a risk-based requirement that is driven by the composition of an institution's loan and investment portfolio and other operating characteristics, and a minimum capital requirement that ensures some capital cushion regardless of the outcome of the risk-based standard. This is the case for Fannie Mae, Freddie Mac and the FHLBanks, where risk-based and minimum capital requirements are established by law.

The Committee should be mindful that changes in the GSEs' capital requirements have a direct impact on the availability and cost of mortgages in the housing finance system. Higher capital requirements limit GSE activity, reduce the range of GSE products and programs (impairing the ability to serve low- and moderate-income borrowers) and increase the cost of mortgage borrowing. Capital requirements that exceed those dictated by the risk of GSE activities and operations unnecessarily reduce the flow of capital to the housing finance system and add unnecessarily to the cost of those funds. The result would be a significant setback to current efforts to expand affordable homeownership and rental housing opportunities.

There is fairly widespread agreement that the new GSE regulator must have much greater authority to adjust capital requirements than the current regulators possess. Concepts and systems for determining risk-based capital requirements have evolved significantly since statutory requirements for Fannie Mae and Freddie Mac were established and it is argued that the current specificity of the statute in this area makes it difficult, if not impossible, for the regulator to adopt and maintain a state-of-the-art risk-based capital framework. The most debated policy questions, however, appear to be whether the minimum capital requirements should remain unchanged in statute and what degree of authority should be granted the new regulator to adjust the minimum requirements.

NAHB agrees with the approach taken in H.R. 1427, which would give the GSE regulator full authority to establish and adjust the risk-based capital system as the state of the art evolves. NAHB supports the removal of the current statutory criteria governing risk-based capital requirements for Fannie Mae and Freddie Mac to allow the new regulator full freedom to establish and adjust such standards through regulation. Comparable authority should be granted to the regulator with regard to the risk-based capital requirements of the FHLBanks.

Minimum capital requirements are intended to function as a backstop to risk-based systems and NAHB believes the minimum standard for the GSEs should continue to serve that purpose. NAHB does not support the imposition of bank minimum capital requirements on the GSEs, since the portfolios of the GSEs contain primarily residential mortgage-related assets that, historically, have proven to be low-risk. Indeed, the chart attached to the end of this statement shows that residential mortgages have the lowest charge-off rates compared to other assets held by financial institutions. NAHB also believes that the GSE capital requirements should address only risks that are internal to the GSEs, not external risks such as systemic risk in the financial sector.

NAHB supports maintaining the current statutory minimum capital requirements as is done in H.R. 1427. Further, we support authority for the GSE regulator to adjust minimum capital requirements, as long as such adjustments are justified by changes in actual or perceived risk to a GSE and do not unnecessarily impair the GSEs' ability to achieve their mission. In that regard, NAHB appreciates that H.R. 1427 establishes criteria for temporary increases in minimum capital that are exclusively focused on safety and soundness of the GSEs. NAHB also appreciates that H.R. 1427 accommodates concerns about the possible impact of capital provisions on mission by providing for a process where temporary capital increases would be regularly reviewed and returned to the statutory level once the "triggering" issue or issues are resolved. The bill states that temporary increases in capital "shall not remain in place for a period

of more than 6 months unless the Director makes a renewed determination of the existence of an unsafe and unsound condition.”

NAHB supports the fundamental principle that adjustments to minimum capital requirements must be temporary and that the regulator should deal with longer-term risks through the risk-based system. In addition, all changes to GSE capital – risk-based and minimum – should be undertaken through proposed regulation that provides public notice and comment, except in emergency situations, where increases could be instituted and then reevaluated in a subsequent review and comment protocol.

Portfolio Limits

Proposals to arbitrarily limit or reduce the portfolios of Fannie Mae and Freddie Mac are misguided and would have significant adverse effects on the housing finance system. Both Fannie Mae and Freddie Mac hold sizeable portfolios of mortgages and mortgage-backed securities, which play an important role in stabilizing the supply and reducing the cost of housing credit.

First, the portfolios support the provision of mortgage credit through instruments, such as multifamily mortgages and various homeownership loans designed for lower-income borrowers that are not attractive to secondary market investors and, therefore, cannot be packaged and sold in mortgage-backed securities. Such products are expanding as more focus and requirements are placed on the GSEs to address the housing finance needs of more difficult to reach segments of the population.

Second, the GSE portfolios have served as an important shock absorber for housing borrowers in times of economic crisis. This is evidenced by the relative stability in mortgage availability and interest rates as other sectors of the financial markets were experiencing severe volatility in credit availability and cost during the 1998 international debt crisis and again following the 9/11 terrorist attacks in 2001. Most recently, the portfolios of Fannie Mae and Freddie Mac allowed them to play a major role in efforts to rebuild housing and other pressing housing finance needs in the Gulf Coast areas that suffered hurricane devastation in 2005. Fannie Mae and Freddie Mac stepped up their portfolio purchases to stabilize the mortgage markets in all of these periods and mortgage credit remained available at affordable rates.

Third, the added demand from Fannie Mae’s and Freddie Mac’s portfolio purchases helps to lower yields on mortgage-backed securities which flow through to lower rates on the underlying mortgages. Some have argued that removing Fannie Mae and Freddie Mac as buyers in this market would have no impact on mortgage borrowing costs. NAHB believes that such a position ignores the basic economic principle of supply and demand. Cutting GSE portfolio holdings by more than a trillion dollars, as some have proposed, would certainly have a major adverse impact on mortgage rates, even if the reduction were phased in over a number of years.

Finally, GSE portfolio operations have facilitated an expansion of investors in the U.S. housing markets. Foreign investors are supplying increasing amounts of capital for residential mortgages in this country through purchases of GSE debt and currently account for a significant portion of

such holdings. Some foreign investors are reluctant to invest in mortgage-backed securities, primarily due to unfamiliarity with fixed-rate, long-term mortgage collateral and concern over prepayment risk on such loans. The GSEs have successfully negotiated this obstacle by purchasing and holding mortgage-backed securities through funding provided by sales of their debt to foreign investors. GSE portfolio restrictions, therefore, would constitute a major setback to successful efforts to broaden the sources of capital for the U.S. housing markets.

NAHB recognizes that Fannie Mae and Freddie Mac also are able to generate profits through their portfolio operations by virtue of the spread between their advantaged borrowing costs and market yields on mortgage-backed securities. NAHB shares the concern that has been expressed that such profits have been directed too extensively to GSE shareholders and executives. However, NAHB believes the best way to address this is not through restricting and shrinking GSE portfolios. Such actions would undercut the GSEs' ability to continue the pursuit of the valuable results outlined above. Instead, NAHB believes that the recommendations contained elsewhere in this statement to toughen GSE affordable housing requirements, including mandating annual Fannie Mae and Freddie Mac contributions to an Affordable Housing Fund, would succeed in more effectively directing GSEs' portfolio profits to mission purposes.

With regard to safety and soundness, the new regulator should hold each GSE accountable to have the strategies, systems, personnel and capital that are adequate to fully mitigate any risk to the Enterprises associated with the holding of mortgages and mortgage-backed securities as well as other portfolio investments. This would include the establishment of risk-based capital requirements to provide appropriate capital coverage for all portfolio-related activities. In addition, review of portfolio functions and operations should be an integral part of the regular safety and soundness examinations conducted by the regulator. Specific limits on the GSEs' portfolios therefore are overreaching and unnecessary in addressing their safety and soundness.

On that basis, NAHB supported the approach in the bill approved by the House in the 109th Congress, where the regulator would be granted authority to oversee the on-balance sheet and off-balance sheet assets and liabilities of each Enterprise and, based on such reviews, require an Enterprise to dispose of, or acquire, any asset or liability if the regulator determines that such action is consistent with the safe and sound operation of the Enterprise. The House-approved bill also directed the regulator, within a year, to submit a report to Congress that would include a description of Fannie Mae's and Freddie Mac's portfolio holdings; an analysis of the risk implications for the Enterprises of such holdings, and the effectiveness of risk management measures undertaken by the Enterprises to address such risks; an analysis of portfolio holdings for safety and soundness purposes; an assessment of whether portfolio holdings fulfill the Enterprises' mission purposes; and, an analysis of the potential systemic risk implications of the portfolio holdings for the Enterprises, the housing and capital markets, and the financial system as well as whether such holdings should be limited or reduced over time.

In contrast, H.R. 1427 requires the regulator to issue regulations, within 180 days, that establish standards for evaluating whether the portfolio holdings of Fannie Mae and Freddie Mac, or rate of growth of those portfolio holdings, are consistent with the mission and the safe and sound operations of the Enterprises. The bill sets forth a list of factors that the regulator must consider in developing these standards:

1. The size or growth of the mortgage market;
2. The need for the portfolio in maintaining liquidity or stability of the secondary mortgage market;
3. The need for an inventory of mortgages in connection with securitizations;
4. The need for the portfolio to directly support the affordable housing mission of the Enterprises;
5. The liquidity needs of the Enterprises;
6. Any potential risks posed by the nature of the portfolio holdings; and
7. Any additional factors the regulator determines to be appropriate.

As in the House bill passed in the 109th Congress, H.R. 1427 grants the new regulator authority to oversee Fannie Mae's and Freddie Mac's portfolios and to require the disposition, or acquisition, of assets. In a positive addition, as advocated by NAHB, H.R. 1427 grants the regulator the leeway to make temporary adjustments to the established portfolio standards to allow the Enterprises to support the mortgage and housing markets during times of economic distress or market disruption.

NAHB appreciates that the provisions in H.R. 1427 contain no specific limits or criteria mandating huge reductions in the GSEs' portfolios. The provisions also do not directly reference the term "systemic risk," which has been a rallying cry for those advocating major shrinkage in the Enterprises' portfolios. Nevertheless, the vagueness of the last two criteria on the list of factors to be considered by the regulator in issuing portfolio regulations has led NAHB's members to express concerns that such language could be subject to overly broad interpretation and could be employed to unnecessarily constrain the portfolio activities of Fannie Mae and Freddie Mac to the detriment of mortgage market stability and the Enterprises' pursuit of their housing mission. These concerns were heightened significantly by recent remarks by Federal Reserve Chairman Ben Bernanke, where he advocated requiring Fannie Mae and Freddie Mac to focus their portfolios almost exclusively on holdings of mortgages or mortgage-backed securities that support affordable housing. The Wall Street Journal reported that, "if implemented, Mr. Bernanke's suggestion would entail drastic reductions in the companies' portfolios."

NAHB would like to see revision of H.R. 1427's portfolio criteria language to prevent such an outcome.

Program Approval

An important part of the mission oversight responsibilities of a GSE regulator is the review of activities to ensure conformance with a GSE's charter and public purpose. In addition to providing liquidity and lowering borrowing costs in the housing finance system, the housing-related GSEs support innovation in mortgage products and programs as well as technological improvements that address housing needs. In considering a new GSE regulatory regime, a key challenge involves developing a program review and approval process that is sufficiently rigorous to ensure charter compliance, support for achievement of affordable housing goals, and safety and soundness while facilitating the GSEs' ability to continue to engage in program, product and technological innovation to address market needs in a timely manner.

NAHB supports a program approval process for the Enterprises which ensures that they are operating within their charters and undertaking activities in a safe and sound manner. The program approval process should also accommodate innovation and prompt responses to market needs. To accomplish that, program oversight should focus on broad categories of programs and should not involve micromanagement of individual activities within an approved program area.

Prior approval should only be required for new “programs” that represent broad areas of “products” and/or “activities” that are significantly different from those previously undertaken. New activities under previously approved programs should not require prior approval. However, the regulator should be notified in advance before a new activity under an approved program is undertaken. Review of previously approved programs and activities should occur only as a part of safety and soundness supervision. The regulator should be granted a reasonable, but limited period of time for review of new programs submitted for prior approval.

The key criteria in the program approval process should be whether a program is permitted under a GSE’s charter and needed to facilitate achievement of mission, including affordable housing goals. Safety and soundness of new activities should be a factor only if it is determined that the nature or scope of the activity cannot be adequately addressed through risk-based capital requirements and that the proposed activity poses a significant threat to the financial health of the GSE.

NAHB is concerned that the product approval provisions in H.R. 1427 could open the door to unneeded interference with the development of products and activities that are within the GSEs’ charters. Further, the approval standards called for in H.R. 1427 – particularly the impact on the mortgage finance system – goes beyond safety and soundness and housing mission principles. The net effect of this burdensome process will be to slow or impede the Enterprises’ ability to respond to changing market needs. NAHB supports the program approval approach in the 2005 House bill, which retained the current law definition of new program and did not require a market impact test.

NAHB is pleased, however, that H.R. 1427 excludes from the definition of product existing automated underwriting systems and modifications to mortgage terms and conditions or underwriting criteria for mortgages purchased by the Enterprises. NAHB also applauds the decision not to include language establishing a “bright line” boundary between primary and secondary market activities in H.R. 1427. Bright line language, such as that contained in legislative proposals introduced in the 109th Congress, would be disruptive to the operation of the secondary market, stifle innovation and lead to higher mortgage costs. The Enterprises’ charters already clearly define their mission and functions. It is redundant to require regulations to define the primary and secondary mortgage markets as provided for in the 2005 House-passed bill. NAHB is pleased that the provision was dropped in H.R. 1427.

Conforming Loan Limits

By their charters, Fannie Mae and Freddie Mac are restricted to purchasing mortgages with loan amounts at or below their statutory loan purchase limit, referred to as the “conforming” loan

limit. The conforming loan limit is increased annually on the basis of the annual percent change in the average home price index computed by the Federal Housing Finance Board (FHFB). The loan limit ceiling is 50 percent higher in Alaska, Hawaii, Guam and the U.S. Virgin Islands to account for higher housing costs in these areas.

Loans with initial balances equal to or less than the conforming loan limit typically carry interest rates of 25 or more basis points less than non-conforming loans. A 25 basis point difference might not appear at first to be significant, however, NAHB estimates that almost 1.2 million U.S. households would be priced out of the housing market if mortgage interest rates increased from 5.75 percent to 6.00 percent!

NAHB supports the current statute, which only allows for percentage increases in the conforming loan limit that correspond to increases in the underlying index. NAHB opposes provisions contained in H.R. 1427 that would permit the conforming loan limit to decrease in proportion to a year-to-year decline in the Federal Housing Finance Agency home price index. A mechanism such as the one proposed would disrupt mortgage markets and, considering the length of the mortgage process, would be a source of apprehension among borrowers. The conforming loan limit has been held at the previous year's level in those years when the index has declined and these decreases have been netted out of increases in subsequent years. This system has worked well and has provided stability in times when the home price index has increased, as well as when it has decreased.

The current statutory system, however, inhibits origination of conforming loans in states where average home prices exceed the conforming loan limit. Thus, borrowers in these states cannot benefit from lower rates on conforming loans. To rectify this situation, NAHB supports the high-cost area provisions in H.R. 1427 that would allow the conforming loan limit in high cost areas to be equal to the median home price up to 150 percent of the national loan limit. This provision recognizes that special consideration should be given to mortgage borrowers who live in areas that have relatively high house prices.

However, NAHB cautions that the high cost area provision should be based on statewide median home prices. Applying the high cost definition to areas smaller than states could have the unintended consequence of giving states not typically considered high cost areas a benefit only truly needed in more limited geographies.

NAHB also has reservations about restricting the conforming loan limit for high cost areas to mortgages which are securitized and sold. Ultimately, borrowers are unaware of the workings of the secondary market for mortgage loans. These borrowers should not be affected differently if a loan is targeted to be held in a GSE's portfolio or if a loan will be used as collateral for a mortgage-related security.

Affordable Housing Requirements

NAHB believes the housing GSEs can and should do more to accomplish their affordable housing mission. The affordable housing requirements for Fannie Mae, Freddie Mac and the FHLBanks should be strengthened to ensure a more effective and targeted transfer of GSE

benefits to the housing marketplace. Such changes, however, should not be undertaken in a manner that impairs the GSEs' ability to achieve their mission of providing liquidity to the mortgage markets.

Presently, Fannie Mae and Freddie Mac are required by law to meet annual housing goals established by the Department of Housing and Urban Development (HUD). The housing goals track Fannie Mae's and Freddie Mac's purchases of mortgages for low- and moderate-income people (the low/mod goal); loans in underserved geographically targeted areas (the underserved areas goal); and, mortgages for very-low income people and neighborhoods (the special affordable goal). Each of the 12 FHLBanks is required by law to contribute at least 10 percent of its annual net earnings to an Affordable Housing Program (AHP). The AHP subsidizes the cost of housing for very-low-income and low- or moderate-income owner-occupied and rental housing. The subsidy may be in the form of a grant ("direct subsidy") or a below-market interest rate on an advance (loan) from the FHLBank to a member lender.

Affordable Housing Goals for Fannie Mae and Freddie Mac

NAHB supports the proposed revisions to the affordable housing goals for Fannie Mae and Freddie Mac outlined in Section 125 of H.R. 1427. The proposed language is a significant improvement over current housing goals regulation and adopts several of NAHB's previous recommendations.

Single-Family Housing Goals

Housing goals levels should continue to be established through regulations that incorporate general statutory criteria. NAHB supports the use of HMDA data as a benchmark for setting the single-family housing goals. We also are pleased that the Committee has eliminated "ability of the Enterprises to lead the industry" as a factor in establishing higher goals than those based solely on HMDA.

In addition, NAHB supports the tighter income definitions in H.R. 1427. Lowering the percent of area median income thresholds used in the definitions of low-income, very low-income and low-income areas, as well as establishing an extremely low-income definition will focus the Enterprises more directly on lower-income populations. NAHB believes that more narrowly tailored income definitions will result in more concentrated efforts by the GSEs and expand affordable homeownership and rental housing opportunities to people and areas most in need.

Further, we support the decision to focus the single-family goals on purchase money mortgages, excluding refinance mortgages from the goals calculations. The volatility of refinancing activity has a significant impact on the ability of the Enterprises to meet the housing goals without disrupting the secondary market. Refinancing volume is driven by interest rate fluctuations, not by enterprise outreach activities. Removing single-family refinance transactions from the goals calculations will eliminate these negative effects and will focus Fannie Mae's and Freddie Mac's activities directly on supporting affordable housing home purchase transactions. For these same reasons, we question the need for a refinance subgoal under the low-income single-family housing goal. The volatility of interest rates and refinancing activity will make it difficult to

establish an annual target *a priori* and could dilute the Enterprise's focus on purchase money mortgages.

Multifamily Special Affordable Housing Goal

NAHB supports the proposed definition of the multifamily special affordable housing goal in H.R. 1427. In particular, we support the expansion of the current statutory definition to include dwelling units assisted by the low-income housing tax credit as well as credit for units financed by Housing Finance Agency (HFA) bonds. These provisions address serious shortcomings in the present housing goal statute which does not permit such investments to be counted as goals-qualifying activities. These instruments finance much of the newly built multifamily rental housing that is affordable to households with low- and moderate-incomes. Thus, the Enterprises should get goals credit for purchases of mortgages on properties that were financed with these instruments.

Further, NAHB strongly supports the additional requirements for smaller projects, particularly for projects of 5 to 50 units. These units are key sources of affordable housing for large numbers of low- and moderate-income households, first-time homebuyers and minorities. NAHB has long supported improved financing mechanisms for small projects. Financing for small projects often is difficult to obtain and relatively expensive compared to financing costs for larger projects. Small project loans are generally made by portfolio lenders who hold the loans in portfolio. Given the importance of small projects in providing affordable housing, HUD provided bonus points for the GSEs' purchase of such loans in its 2001-2003 Housing Goals rule. The bonus points system worked as the GSEs doubled their purchases of small multifamily loans during this time. Unfortunately, HUD eliminated the bonus point system in the current housing goals rule and the GSEs' focus on smaller properties has waned. Establishing small projects requirements will re-focus the GSEs on this important source of affordable housing.

NAHB recommends that the additional small property requirements should be extended to include 2- to 4- unit owner-occupied and investor-owned rental properties. These properties were also included in HUD's bonus points system since these are also an important source of affordable housing, but have weak secondary market support.

Duty to Serve Underserved Markets

NAHB supports the provisions in H.R. 1427 that establish a duty for the Enterprises to serve underserved markets. Specifically, these provisions direct the Enterprises to develop products and engage in activities to reach the most difficult underserved housing markets, including manufactured housing, affordable housing preservation, rural and other underserved markets. NAHB notes that these provisions will encourage the Enterprises to expand beyond better-served markets, similar to the bonus point system under HUD's 2001-2003 housing goals rule. NAHB believes that the proposed underserved markets requirements will work in a similar way as a means to direct GSE purchases toward specific market segments. NAHB recommends, however, that the list of underserved markets should be expanded to include very low-, low- and moderate-income first-time and minority home buyers.

Affordable Housing Fund for Fannie Mae and Freddie Mac

As stated earlier, NAHB strongly supports the creation of an affordable housing fund established through annual contributions by Fannie Mae and Freddie Mac and modeled on the statutorily prescribed Affordable Housing Program (AHP) of the Federal Home Loan Bank System. Such a fund would, in combination with more challenging housing goals standards, raise the bar for Fannie Mae's and Freddie Mac's mission activities to more effectively channel benefits of their GSE charters to serve housing needs that are currently unmet. The goal of the fund is to support activities that cannot be undertaken as part of Fannie Mae's and Freddie Mac's traditional lending and investment business.

NAHB is pleased to see that H.R. 1427 establishes an Affordable Housing Fund (AHF). The focus of this fund is to increase affordable homeownership and rental opportunities for very-low and extremely-low income households, increase and preserve the supply of housing for such households and support infrastructure development in connection with housing. In addition, the AHF would seek to leverage investments from other sources to support development financed by AHF grants. NAHB supports this framework.

Calculation of the GSEs' Contribution

NAHB believes that the calculation of the GSEs' annual contribution to the AHF should provide a relatively stable flow of funds. H.R. 1427 provides that contribution amounts equal to 1.2 basis points on each Enterprise's total outstanding mortgages (including those held in portfolio and those backing securities) would be required each year. NAHB supports this provision, as it should result in less volatility in annual fund contributions than previous proposals for calculating the Enterprises' contributions.

Administration of the Fund

H.R. 1427 removes Fannie Mae and Freddie Mac from managing the AHF, which is a major change from the bill passed by the House in the 109th Congress. Rather, funds would be distributed to states in block grants based on a formula developed by HUD. The states would decide which of its agencies (e.g., the state housing finance agency, housing and community development entity, or tribally designated entity) should administer the program and allocate the grants. Each state is required to develop an allocation plan for the distribution of the grants, based on priority housing needs, in accordance with the regulations that are to be established for the program. In addition, the states are required to notify the public of the establishment of the plan and provide an opportunity for public comment.

NAHB's primary concern regarding the administration of the AHF is that the funds are distributed fairly. The allocation process for individual applications should ensure that funding goes to the projects providing the most and highest quality housing meeting the needs identified by the states. The allocation criteria should also ensure that only qualified, experienced sponsors are awarded funds. NAHB members report that under many current housing programs, state allocation criteria produce a bias in favor of nonprofits. Our members feel that the allocation criteria fail to consider whether sponsoring entities have sufficient experience to undertake and

sustain affordable housing development and management activities. NAHB believes that this bias, by excluding companies with strong experience and capacity in efficient housing production, undercuts the effectiveness and diminishes the results of these programs. Applications for funding should be judged on the merits of the housing to be produced, not on the tax paying status of the sponsoring company.

Eligible Activities

NAHB supports the proposed eligible activities as set forth in H.R. 1427. NAHB also supports the requirement that not less than 10 percent of a grantee's allocation be used for homeownership activities. Homeownership applications are often at a disadvantage in a competitive process because it is more difficult to serve households at the very lowest income levels through homeownership projects, and most such proposals consist of smaller numbers of units.

NAHB also supports the list of prohibited uses as provided in H.R. 1427. NAHB strongly believes that the funds should be used for direct housing production and preservation activities, rather than the administrative costs of grantees or other activities not directly related to the specific project.

Eligible Recipients

As mentioned above, NAHB strongly believes that the allocation process should not contain a bias against participation by for-profit companies. We strongly believe that companies with proven experience and capacity for carrying out housing development meeting stated needs should be considered the best candidates for the grants, regardless of their tax status. NAHB, therefore, appreciates the fact that H.R. 1427 includes for-profit, nonprofit and faith-based organizations as eligible recipients of AHF grants. NAHB also supports the bill's direction that recipients must demonstrate a capacity for carrying out the activities that are to be funded by the grant, as well as make assurances that they shall comply with all regulations and requirements of the program.

NAHB suggests that the language related to the qualities of the sponsor be strengthened to ensure that sponsors have a demonstrated successful track record of carrying out similar activities, as well as the capacity to undertake new activities. In addition, for rental projects, sponsors should have demonstrated success in the management of affordable housing properties. Strong management capabilities are critical to the success of affordable rental properties over the long-term.

Accountability of Grantees and Recipients

H.R. 1427 requires the grantees to provide annual reports to the Director describing the activities funded and the manner in which they complied with its allocation plan during the year. The Director is required to make these reports available to the public. H.R. 1427 establishes penalties to be imposed on grantees that fail to comply substantially with their allocation plan, including a reduction of the amount of assistance, repaying of any amounts determined to have been misused and limiting the availability of funding to the grantees.

To further ensure the most appropriate and effective use of program funds, NAHB continues to advocate for the creation of an Affordable Housing Advisory Council, which would assist the regulator in evaluating whether the purposes of the AHF are satisfied, as well as overseeing the competitive equity of the fund distribution process and the system for scoring fund applicants. The council members should include a cross-section of affordable housing industry professionals, including for-profits, nonprofits and government agencies. The creation of a council would increase the transparency of the grant-making process and provide the public with additional access to information about the AHF, its mission, activities and results.

Revisions to the FHLBank Affordable Housing Program

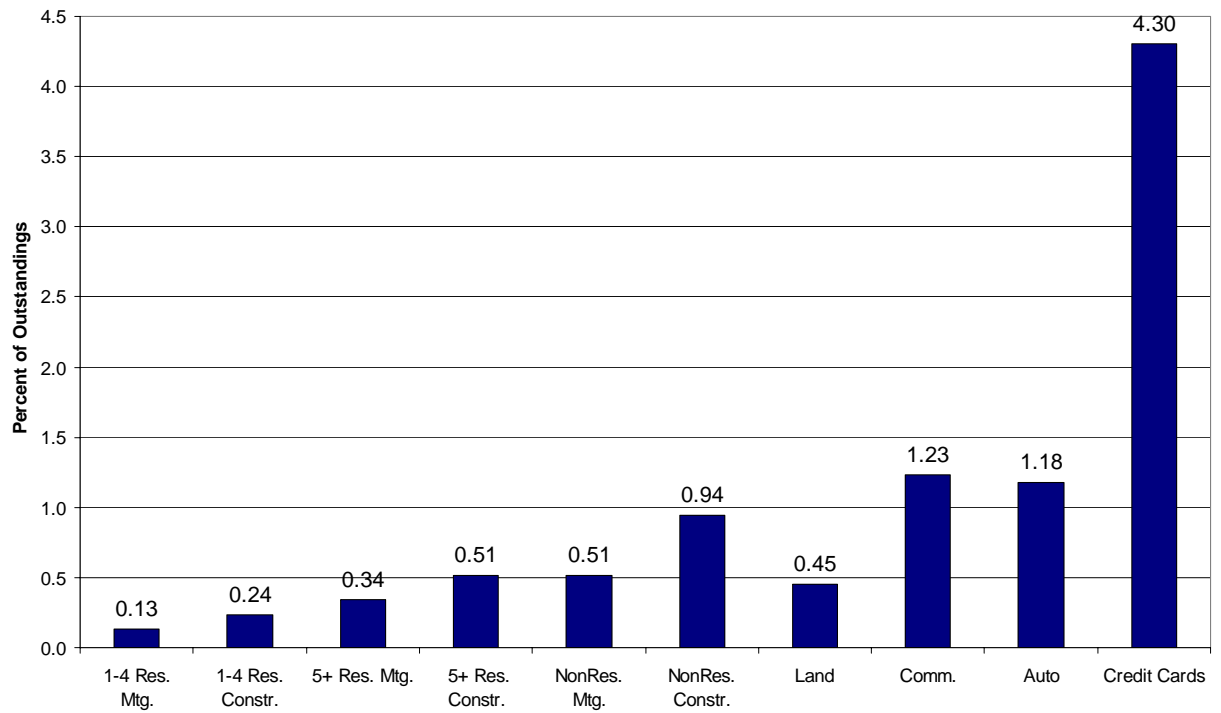
NAHB recommends revising the statute for the Federal Home Loan Bank Affordable Housing Program (AHP) in order to remove the current statutory priority for allocations to nonprofit sponsors in the competitive selection criteria. This part of the law has impeded participation by NAHB's members in the AHP and, as we have stated, the exclusion of capable and experienced for-profit housing producers needlessly works against the goal of providing housing most efficiently in areas where it is needed most.

Conclusion

NAHB appreciates the opportunity to share our views on the world-class regulation of Fannie Mae, Freddie Mac and the Federal Home Loan Banks, the housing GSEs. It goes without saying that the GSEs have been and continue to be critical components of the nation's housing finance system, a system without equal anywhere in the world and one that contributes so much to the national economy. These entities were chartered to uphold an important public purpose and must be held accountable for actions that violate that public purpose or erode confidence in the GSEs or their mission.

NAHB is pleased to be part of the process to improve a clearly lacking oversight system, establish a world class regulator and ensure that the GSEs continue to expand housing opportunities for American families. We believe that this process can be a success without undercutting the GSEs' housing mission if the following areas are addressed: one, balance housing with safety and soundness concerns; two, employ capital as a precise instrument of risk management; three, preserve GSE portfolios as tools for achieving liquidity and affordable housing mission; four, maintain the GSEs' flexibility to respond promptly, within their charters, to market needs; five, raise the conforming loan limit in high cost areas; and, six, focus and enhance GSE benefits to expand affordable housing opportunities. NAHB looks forward to working with the Congress to use these principles to achieve our mutual goals as the legislative process moves forward.

Comparison of Net Chargeoff Rates by Loan Type for All OTS Thrifts
Annual Averages, 1990-2006



Source: Office of Thrift Supervision; Compiled by NAHB